

FUNCTION 650: SOCIAL SECURITYMAJOR SPENDING CHANGES PROPOSED FOR BUDGET FUNCTION 650:
SOCIAL SECURITY (By fiscal year, outlays in billions of dollars)

Item	1988	1989	1990	1991	1992	Cumulative Five-Year Changes
CBO Baseline	221.0	235.6	252.2	269.9	288.2	
Proposed Changes	-0.1	-0.2	-0.4	-0.4	-0.5	-1.6
President's 1988 Budget as Estimated by CBO	220.8	235.4	251.9	269.5	287.7	
President's 1988 Budget	219.4	232.5	246.8	261.5	275.5	
CBO Reestimates	1.4	3.0	5.1	8.0	12.2	29.7

Proposed Policy Changes

Although the Administration proposes no changes in Social Security benefits, the President's proposals would result in small reductions in outlays in this function during the next five years. The budget incorporates a continuation of the personnel reductions proposed in the last several budgets. In addition, the budget includes one change in the administration of the Social Security program and several changes in coverage under the payroll tax that would affect benefit payments slightly through 1992. The combined effect of these initiatives would save about \$149 million in 1988 and about \$1.6 billion over the next five years.

The staffing levels proposed by the President would reduce the Social Security Administration's (SSA) full-time equivalent (FTE) employment by 2,454 from 1987 to 1988, and by about 11,799 FTEs over the next five years. The proposed 1988 staffing level is about 92 percent of SSA's actual 1986 employment, and about 85 percent of that which prevailed in 1982.

With respect to administrative changes that would affect benefit payments, the SSA would alter its method of selecting for review Disability Insurance (DI) award decisions made by state agencies. The Administration's plan would replace the current selection procedure, which is essentially random, with one that would focus resources on cases where errors in the determination process are most likely to occur. As a result, future benefit payments would be affected, but by only \$34 million over the next five years.

The proposed changes affecting Social Security revenues (discussed in further detail in Chapter III) would increase future benefit payments by covering more earnings under the payroll tax. In particular, coverage of inactive duty training for reservists in the Armed Forces would raise covered earnings for those workers affected and increase the eventual benefits received by most of these workers. Over the next five years, the additional benefits would be negligible (less than \$5 million).

CBO Reestimates

CBO has reestimated the President's budget request upward by a total of \$29.7 billion for the 1988-1992 period. Most of the difference (nearly 90 percent) results from the higher cost-of-living adjustments (COLAs) in the CBO economic assumptions: the Administration forecasts falling inflation over the next five years, while CBO expects inflation to stabilize between 4 percent and 4 1/2 percent.

Social Security Cost-of-Living Adjustments Assumed by CBO and the Administration (In percents)

	<u>1988</u>	<u>1989</u>	<u>1990</u>	<u>1991</u>	<u>1992</u>
CBO	4.1	4.3	4.4	4.3	4.3
Administration	3.5	3.6	3.6	3.1	2.7

CBO also assumes that the number of people receiving disability benefits will increase at a faster rate than the Administration, with the difference amounting to about 60,000 beneficiaries by 1992. This technical estimating difference adds \$1.8 billion over five years to projected program costs.

FUNCTION 700: VETERANS' BENEFITS AND SERVICESMAJOR SPENDING CHANGES PROPOSED FOR BUDGET FUNCTION 700:
VETERANS' BENEFITS AND SERVICES

(By fiscal year, outlays in billions of dollars)

Item	1988	1989	1990	1991	1992	Cumulative Five-Year Changes
CBO Baseline	27.4	27.7	28.2	28.6	28.9	
Proposed Changes						
Loan Guaranty						
Increase origina- tion fee	-0.4	-0.3	-0.3	-0.3	-0.3	-1.6
Sell loan portfolio	-0.2	-0.1	-0.1	0.2	0.2	<u>a/</u>
Medical Care	-0.2	-0.2	-0.3	-0.3	-0.3	-1.4
New GI Bill	0.2	0.1	<u>a/</u>	<u>a/</u>	-0.1	0.2
Other	<u>a/</u>	<u>-0.1</u>	<u>-0.1</u>	<u>-0.1</u>	<u>-0.1</u>	<u>-0.5</u>
Total	<u>-0.7</u>	<u>-0.6</u>	<u>-0.8</u>	<u>-0.6</u>	<u>-0.6</u>	<u>-3.3</u>
President's 1988 Budget as Estimated by CBO	26.7	27.1	27.4	28.0	28.3	
President's 1988 Budget	27.2	27.6	28.0	28.6	29.0	
CBO Reestimates	-0.4	-0.5	-0.6	-0.6	-0.7	-2.9

a. Less than \$50 million.

Proposed Policy Changes

The President's 1988 budget for veterans' benefits and services proposes significant changes in the home loan guaranty program of the Veterans Administration (VA), as well as reductions in veterans' medical care and education benefits.

Loan Guaranty Revolving Fund. The President's 1988 budget proposes to increase the origination fee required of veterans and others obtaining VA guaranteed and direct loans from its current level of 1.0 percent of the mortgage principal to 2.5 percent. This increase would produce net outlay savings of \$1.6 billion over five years. Increases in the loan origination fee were also proposed by the President in his 1986 and 1987 budget requests but were not approved by the Congress.

Also included in the President's budget is a policy change to sell to the public the VA's portfolio of direct loans. These loans, called vendee loans by the VA, were made by the agency to market properties acquired through foreclosure of VA-guaranteed loans. While the VA routinely sells vendee loans for which payments are current, the President also proposes to sell loans that have previously been considered unavailable for sale because of default or poor documentation. Even though this change would not require Congressional action, it is a significant policy change and is therefore not included in the CBO baseline.

In a separate but related change, the President's budget indicates that all vendee loan sales after 1987 will be made without recourse to the government in the event of default. In the past, the VA has guaranteed that loans that default after their sale would be repurchased by the agency. The CBO baseline also assumes loan sales without recourse.

Medical Care. Reductions from baseline spending levels also are proposed by the President for the medical care services provided by the Veterans Administration. The estimated outlay savings over five years would total \$1.4 billion.

As part of the Consolidated Omnibus Budget Reconciliation Act of 1985 (Public Law 99-272), the Congress approved a number of changes in eligibility for VA health care. Certain groups of veterans--such as those with service-connected disabilities--and veterans with annual incomes below \$15,000 per person (\$18,000 per couple) are now entitled to VA health care. Veterans with annual incomes below \$20,000 per person (\$25,000 per couple) are eligible for free care on a space-available basis. Veterans with incomes above these levels are also eligible for care on a space-available basis but are charged copayments for such care. The President's budget would eliminate funding for this last category of veterans. The VA, however, maintains that the required spending cuts can be achieved through reductions in non-essential personnel and other expenses, with little change to the anticipated hospital patient load.

New GI Bill. The President is proposing to reauthorize the All-Volunteer Force Assistance program (New GI Bill) beyond the current June 30, 1988 expiration date. The CBO baseline also assumes the extension of this program. In addition, the President proposes to transfer funding of the basic \$300 monthly benefit from the VA to the Department of Defense (function 050). While this shift would have no impact on budget totals, it would cause a net increase in function 700 outlays, because the current receipts from contributions are greater than current expenditures for benefits.

Compensation. Even though the compensation program is not indexed by law, its benefits historically have been increased for inflation each year through legislation. The CBO baseline includes these out-year inflation increases as a reflection of Congressional policy, and the President's budget proposes to index these benefits permanently. The President, however, assumes significantly lower cost-of-living adjustments (COLAs) than are reflected in the CBO baseline. Under CBO economic assumptions, outlays from compensation COLAs would be \$1.2 billion higher over five years than under assumptions of the Office of Management and Budget (OMB).

CBO Reestimates

In the Loan Guaranty Revolving Fund, CBO assumes that the recent downward trend in defaults will accelerate as the economy improves. The OMB estimate appears to assume, however, that default rates will continue to be high. Because of these different assumptions, CBO's outlay estimates are \$1.8 billion lower than the President's estimates over the five-year period. Lower projections of average benefits in the compensation and pension programs cause CBO estimates to be an additional \$1.2 billion below the President's.

The CBO outlay estimates for 1988 through 1992 in the veterans' education programs are nearly \$300 million below the President's, mainly because CBO estimates that fewer service members will contribute and train under the New GI Bill. The downward reestimate in the New GI Bill is partially offset by an upward reestimate in readjustment benefits, where CBO assumes that fewer veterans would exhaust their entitlement or reach their delimiting date during this period.

Credit Programs

Loan Guaranty Revolving Fund. The changes proposed by the President in the loan guaranty program would have a number of effects on the credit budget. The increase in the loan origination fee to 2.5 percent is expected

to reduce the demand for new guaranteed loans by approximately 7.0 percent; some borrowers will be unable to qualify for a mortgage after the higher fee is added to the mortgage principal, and other borrowers may find conventional financing more attractive. The President is also proposing to sell a higher percentage of acquired properties for cash, rather than financing the sales. This would reduce the number of new vendee loans established.

**MAJOR CREDIT PROGRAM CHANGES PROPOSED FOR BUDGET
FUNCTION 700: VETERANS' BENEFITS AND SERVICES**
(By fiscal year, in billions of dollars)

Item	1988	1989	1990	1991	1992	Cumulative Five-Year Changes
Guaranteed Loan Commitments						
CBO Baseline	24.3	22.2	23.2	24.6	26.0	
Proposed Changes (Loan Guaranty)	-1.6	-1.6	-1.6	-1.7	-1.8	-8.4
President's 1988 Budget as Estimated by CBO	22.7	20.6	21.6	22.9	24.2	
Direct Loan Obligations						
CBO Baseline	1.2	1.1	1.0	0.9	0.7	
Proposed Changes (Loan Guaranty)	-0.1	-0.1	-0.1	-0.1	<u>a/</u>	-0.4
President's 1988 Budget as Estimated by CBO	1.1	1.0	0.9	0.9	0.7	

a. Less than \$50 million.

FUNCTION 750: ADMINISTRATION OF JUSTICEMAJOR SPENDING CHANGES PROPOSED FOR BUDGET FUNCTION 750:
ADMINISTRATION OF JUSTICE

(By fiscal year, outlays in billions of dollars)

Item	1988	1989	1990	1991	1992	Cumulative Five-Year Changes
CBO Baseline	9.1	9.5	9.7	9.8	10.0	
Proposed Changes						
Legal Services						
Corporation	-0.3	-0.3	-0.4	-0.4	-0.4	-1.7
Criminal justice						
assistance	-0.1	-0.3	-0.4	-0.4	-0.4	-1.6
Federal law						
enforcement	0.1	-0.1	-0.2	-0.3	-0.3	-0.8
The Judiciary	0.2	0.2	0.2	0.2	0.2	0.8
General legal activities	0.1	0.1	0.1	0.1	0.1	0.6
Federal prison system	0.1	0.1	0.1	0.1	0.1	0.5
Other	<u>a/</u>	<u>a/</u>	<u>0.1</u>	<u>0.1</u>	<u>0.1</u>	<u>0.3</u>
Total	0.1	-0.3	-0.5	-0.6	-0.6	-2.0
President's 1988 Budget as Estimated by CBO	9.2	9.2	9.1	9.3	9.4	
President's 1988 Budget	9.2	8.9	8.8	8.9	9.1	
CBO Reestimates	<u>a/</u>	0.3	0.4	0.3	0.3	1.4

a. Less than \$50 million.

Proposed Policy Changes

The President's budget proposals would increase funding for the administration of justice in 1988 and maintain spending at close to the 1988 level, but

below the CBO baseline, from 1989 through 1992. Spending on federal law enforcement is projected to decrease slightly, while spending on the judiciary and federal prisons would increase, relative to baseline levels. The elimination of funding for the Legal Services Corporation and justice assistance programs would reduce outlays by \$3.3 billion over the 1988-1992 period and total savings for the function would be \$2.0 billion over the five-year period.

Legal Services and Justice Assistance. The largest savings in the President's budget for function 750 comes from terminating federal funding for the Legal Services Corporation and eliminating certain justice assistance programs. As in previous years, the President proposes to end funding for the Legal Services Corporation, with savings of \$300 million to \$400 million annually relative to the CBO baseline; the five-year savings would be \$1.7 billion. The Administration also proposes to eliminate the Office of Juvenile Justice and Delinquency Prevention, the state and local drug grant program, funds for incarceration of the Mariel Cubans, and regional information sharing, and to limit obligations from the Crime Victims Fund. The cumulative savings from these spending reductions would be \$1.6 billion over the 1988-1992 period, with \$1.2 billion of that amount attributable to the elimination of the drug grant program.

Federal Law Enforcement. The overall spending levels proposed by the Administration for federal law enforcement activities are slightly lower than the CBO baseline from 1988 to 1992. In total, law enforcement spending would be nearly \$75 million (or 1 percent) above the baseline in 1988, but would fall to nearly \$300 million (or 5 percent) below the baseline by 1992. The largest single increase is for the Immigration and Naturalization Service (INS) to implement the Immigration Reform and Control Act of 1986. The President's budget includes a \$147 million supplemental in 1987 and a \$245 million increase in budget authority in 1988 over the current 1987 appropriation. Outlays by the INS would increase by 44 percent in 1988 relative to 1987. The additional spending would cover increased border enforcement, enforcement of employer sanctions, the special agricultural workers programs, and verification programs. The President's budget also includes spending for the legalization program, which will be funded entirely from user fees. The Administration also has proposed a 7 percent increase in spending by the Federal Bureau of Investigation (FBI) for 1988, relative to the baseline. This increase would enable the FBI to purchase advanced equipment for the criminal investigations division and to construct new laboratories.

Funding for the United States Customs Service would be decreased under the President's proposals, primarily because no funds are requested for 1988 to cover activities funded in the Omnibus Drug Supplemental Appropriations Act of 1987. The agency's 1988 funding request is \$110 million, or 10 percent, below the 1987 level. Proposed spending on salaries and expenses for the Customs Service is more than 10 percent below the CBO baseline each year, while spending for the Customs air interdiction program would be more than 50 percent below the baseline by 1992.

Judicial Activities and Federal Prisons. The President's budget includes additional spending for the courts, the Department of Justice's legal activities, and the operation of the federal prison system. Spending by the Judiciary would be approximately \$0.8 billion (or 12 percent) above the baseline level from 1988 through 1992. Within the Department of Justice, the budget includes increases for general legal activities (including the United States Attorneys), the United States Marshals, and the expansion of the United States Trustees Program.

The Administration also proposes to increase spending on the federal prison system by approximately \$500 million above the CBO baseline from 1988 through 1992. Spending for prison construction would decrease slightly relative to the baseline over this period, while spending for salaries and expenses would increase.

CBO Reestimates

Based on historical spending rates, CBO estimates slightly higher outlays (\$1.4 billion over the five-year period) than the Administration for programs in this function.

FUNCTION 800: GENERAL GOVERNMENTMAJOR SPENDING CHANGES PROPOSED FOR BUDGET FUNCTION 800:
GENERAL GOVERNMENT (By fiscal year, outlays in billions of dollars)

Item	1988	1989	1990	1991	1992	Cumulative Five-Year Changes
CBO Baseline	6.9	6.9	7.2	7.4	7.4	
Proposed Changes						
Internal Revenue						
Service	0.4	0.6	0.6	0.5	0.4	2.5
Federal Buildings Fund	0.3	0.5	0.4	0.3	0.3	1.8
Legislative Branch	0.1	0.1	0.1	0.1	0.1	0.5
Federal Financing Bank	0.2	0.2	0.2	0.2	0.2	1.0
Federal Supply Service	-0.2	-0.2	-0.2	-0.2	-0.2	-0.9
Other	<u>0.1</u>	<u>0.1</u>	<u>a/</u>	<u>a/</u>	<u>-0.1</u>	<u>0.1</u>
Total	0.9	1.3	1.1	0.9	0.7	4.9
President's 1988 Budget as Estimated by CBO	7.7	8.2	8.3	8.2	8.1	
President's 1988 Budget	7.5	7.9	7.9	7.9	7.8	
CBO Reestimates	0.2	0.4	0.3	0.3	0.3	1.6

a. Less than \$50 million.

Proposed Policy Changes

The President's budget includes increased funding for general government activities that would result in outlays \$4.9 billion above the baseline over the 1988-1992 period. The largest increase is for the Internal Revenue Service (IRS), to implement the Tax Reform Act of 1986 and to fund several initiatives aimed at increasing revenue collections. These initiatives include hiring additional IRS staff to identify and collect taxes owed but not paid.

The President is requesting a 1988 appropriation for the IRS that is \$0.5 billion above the baseline level. Over the five-year period, IRS outlays would be \$2.5 billion, or 10 percent, above the baseline. The initiatives to increase revenue collections are estimated to produce \$1.8 billion in additional revenues in 1988, and a total of \$14.4 billion over the 1988-1992 period.

The President also proposes to use the increased rental income resulting from the 1988 reappraisal of federal office space to fund expanded building construction, acquisition, and repair projects through the Federal Buildings Fund. Additional spending for these activities would exceed baseline levels by \$1.8 billion over the five-year period. The proposed appropriations for activities of the Legislative Branch would result in outlays that are \$0.1 billion above the CBO baseline each year.

The budget includes a proposal, repeated from the 1987 budget, to show the surplus income of the Federal Financing Bank in the net interest function (900) of the budget rather than in the general government function. This change would increase general government outlays by \$0.2 billion per year, but would have no net effect on the budget.

The major outlay savings estimated for this function involve the General Services Administration (GSA). The President proposes to recover fully the administrative costs of the GSA in supplying goods and services to federal agencies through the General Supply Fund. The GSA currently sells goods and services to agencies at cost, and the administrative expenses of managing this activity are funded by an appropriation to the Federal Supply Service. The budget proposal would eliminate this appropriation, and agencies would cover these expenses by paying a charge above the price of the goods or services they purchase from GSA. As a result, spending would decrease by a total of \$0.9 billion through 1992.

CBO Reestimates

The budget assumes that renewed efforts to identify and sell surplus federal property would raise about \$1.6 billion over the 1988-1992 period. Earlier attempts by the Administration to sell property fell substantially short of stated goals, and the lengthy process of declaring property as surplus makes drastic increases in the inventory of salable surplus property unlikely. CBO therefore estimates that surplus property sales will result in receipts of only \$0.6 billion over the next five years, a slight increase over recent experience. For a number of other programs, CBO has estimated outlays greater than in the budget, based on historical spending patterns.

FUNCTION 850: GENERAL PURPOSE FISCAL ASSISTANCE

MAJOR SPENDING CHANGES PROPOSED FOR BUDGET FUNCTION 850:
GENERAL PURPOSE FISCAL ASSISTANCE
(By fiscal year, outlays in billions of dollars)

Item	1988	1989	1990	1991	1992	Cumulative Five-Year Changes
CBO Baseline	1.9	1.9	2.0	2.0	2.1	
Proposed Changes						
Payments to states, mineral and timber receipts cost sharing	-0.2	-0.3	-0.3	-0.3	-0.3	-1.4
Payments to the District of Columbia	-0.1	-0.1	-0.1	-0.2	-0.2	-0.7
Other	<u>a/</u>	<u>a/</u>	<u>a/</u>	<u>a/</u>	<u>a/</u>	<u>a/</u>
Total	-0.3	-0.3	-0.4	-0.4	-0.5	-2.1
President's 1988 Budget as Estimated by CBO	1.5	1.6	1.6	1.6	1.6	
President's 1988 Budget	1.5	1.5	1.6	1.7	1.7	
CBO Reestimates	<u>a/</u>	<u>a/</u>	<u>a/</u>	-0.1	-0.1	-0.2

a. Less than \$50 million.

Proposed Policy Changes

Changes in payments to states and localities from mineral and timber receipts account for most of the savings in this function. The President proposes to reduce the amount of federal timber and mineral receipts shared with state and local governments by calculating their share after deducting collection costs. Currently the states' and counties' share of such receipts is calculated as a percentage of gross, not net, receipts. These shares vary

from program to program, but most are between 25 percent and 50 percent. CBO estimates that this proposal would result in savings to the federal government of between \$200 million and \$300 million per year, and five-year savings of \$1.4 billion by 1992.

In addition, the President is proposing to reduce the annual basic payment to the District of Columbia from about \$444 million in 1987 to \$425 million a year, resulting in savings of \$0.5 billion relative to the baseline over the 1988-1992 period. The President's budget also reflects a change in the way that the federal government reimburses the District for its use of water and sewer services. Currently, a lump sum appropriation is made to reimburse the District for the costs of providing these services to all federal agencies located within its jurisdiction. Under the President's proposed administrative change, all agencies would be billed for their actual usage. This proposal would have no net effect on the federal budget but would result in outlay savings of about \$40 million a year in function 850. Total savings in payments to the District in this function would total \$0.7 billion over the 1988-1992 period.

The General Revenue Sharing program, which previously accounted for most of the spending in this function, has expired. The CBO baseline does not include any spending for the program, and the Administration does not propose to revive it.

CBO Reestimates

CBO's outlay estimates do not differ significantly from the Administration's estimates for this function.

FUNCTION 900: NET INTEREST

MAJOR SPENDING CHANGES PROPOSED FOR BUDGET FUNCTION 900:
NET INTEREST (By fiscal year, outlays in billions of dollars)

Item	1988	1989	1990	1991	1992	Cumulative Five-Year Changes
CBO Baseline	140.4	146.7	151.5	154.9	153.3	
Proposed Changes						
Debt service	-1.2	-4.0	-7.3	-11.3	-15.6	-39.4
Intragovernmental interest	0.3	0.5	0.8	1.0	1.1	3.7
Federal Financing Bank	-0.4	0.0	0.3	0.3	1.1	1.4
SBA interest	0.0	0.0	0.1	0.1	0.1	0.3
Sale of Bonneville Power Adminis- tration	0.0	0.0	0.0	0.0	0.2	0.2
Other	<u>-0.2</u>	<u>-0.2</u>	<u>-0.2</u>	<u>-0.3</u>	<u>-0.3</u>	<u>-1.2</u>
Total	-1.5	-3.6	-6.3	-10.1	-13.4	-34.9
President's 1988 Budget as Estimated by CBO	139.0	143.1	145.2	144.8	139.9	
President's 1988 Budget	139.0	141.5	139.0	134.8	122.1	
CBO Reestimates	-0.1	1.6	6.2	10.0	17.8	35.4

Proposed Policy Changes

The Administration's proposed spending cuts and revenue increases would reduce federal deficits, borrowing, and debt-service costs. The interest savings grow dramatically over time, from \$1.2 billion in 1988 to \$15.6 billion in 1992. By the end of 1992, debt held by the public would be almost

\$300 billion lower under the President's proposed policies than in the CBO baseline.

A number of federal agencies borrow from--and pay interest to--the Treasury to finance their operations. The interest expense is recorded as a cost to the agency elsewhere in the budget and as an intragovernmental receipt within the net interest function. Changes in intragovernmental interest therefore have no net effect on the deficit. Thus, the Administration's proposals to sell old loans and curtail new lending for these programs reduce interest receipts (and increase net interest outlays) relative to the CBO baseline. The proposed sale of Rural Housing Insurance Fund loans accounts for one-half of the \$3.7 billion loss in interest receipts over the 1988-1992 period. Intragovernmental interest receipts also would be reduced as a result of proposed declines in Treasury borrowing by the Federal Crop Insurance program, housing for the elderly and handicapped, and the Federal Ship Financing Fund.

The President's budget proposes a curtailment of the Federal Financing Bank's (FFB) lending activity. By the end of 1992, total FFB loans outstanding are projected to be \$141 billion under the President's proposals, compared with \$154 billion in the CBO baseline. This difference reflects sales of existing loans as well as sharply decreased future lending. As a result, interest receipts from the FFB are lower than in the CBO baseline--differing only slightly in 1988, but by \$1.1 billion in 1992.

Two other proposed asset sales would also affect net interest. Sales from the loan portfolios of the Small Business Administration (SBA) would reduce interest receipts by \$0.3 billion over the 1988-1992 period. The proposal to sell the Bonneville Power Administration (BPA) in 1991 results in a loss of interest receipts to the Treasury from BPA's borrowing. The loss is \$0.2 billion in 1992. The proceeds from these proposed sales are shown in budget functions 370 and 450 (for SBA), and 950 (for Bonneville).

Other proposals result in small changes in net interest. These include moving the FFB surplus account (loan servicing fees less administrative costs) from general government (Function 800) to net interest and increasing the FFB lending premium from one-eighth of a percentage point to one-half of a percentage point.

CBO Reestimates

Differences in interest rate assumptions lead to a \$40 billion reestimate of the President's net interest outlays over the five-year period. These reestimates range from \$2.5 billion in 1988 to \$15 billion in 1992.

Another \$19 billion in reestimates over the five-year period results from higher deficits than those contained in the President's budget. Because of other reestimates to revenues and outlays, CBO projects that federal government borrowing needs would be higher than those forecast by the Administration. Additional interest costs from this borrowing grow from \$1.1 billion in 1988 to \$5.8 billion in 1992.

The remaining CBO reestimates to the net interest function reduce outlays by \$23.7 billion over the 1988-1992 period. The largest of these reduces outlays for net interest on the public debt by \$11 billion in 1988 through 1992. CBO estimates lower interest costs than the Administration for two major components of the public debt: savings bonds and debt issued to federal government revolving funds. In November 1987, the first group of savings bonds will reach maturity under a market-linked approach inaugurated in late 1982. The switch will make savings bonds accruals more erratic from year to year. CBO's estimates reflect these swings in accruals. The Administration smooths these fluctuations, but in doing so apparently overstates the effective interest rate. The Administration also overstates the current interest rate on public debt securities held by federal government revolving funds such as the deposit insurance funds.

A third downward reestimate for net interest on the public debt stems from different assumptions about means of financing. CBO assumes that the Treasury will borrow less than the full amount of the deficit each year, because it makes explicit assumptions about other means of financing (such as interest accrued but not paid, and issuance of special Federal Deposit Insurance Corporation notes in lieu of cash). Finally, offsetting part of these downward reestimates, CBO makes different assumptions about the mix of Treasury financing. The Administration assumes that roughly half of marketable borrowing will be in short-term Treasury bills, although this would imply rapid escalation in weekly auctions and differs from Treasury's current practice. CBO assumes much greater reliance on medium- and long-term instruments, which carry somewhat higher interest rates.

The largest of the remaining reestimates increases interest from the FFB. Two factors account for most of the increase. First, the Administration's budget omits estimates for prepayment penalties associated with loan asset sales that were mandated by the Omnibus Budget Reconciliation Act of 1986 (Public Law 99-509). Since these penalties are counted as interest, they add \$1.6 billion to FFB interest receipts in 1987. Over the 1988-1992 period, penalties associated with proposed loan asset sales in the Administration's budget add \$2.8 billion to FFB interest receipts. Since these penalties are paid by government agencies, they are offset within other

budget functions and have no effect on the deficit. Second, the budget includes a proposal to allow foreign military credit sales borrowers to prepay their FFB debt without penalty in 1988 and later years. CBO excludes this proposal (see the function 150 analysis in Chapter V) and therefore projects higher FFB interest receipts.

CBO's estimate of interest paid on IRS refunds is lower than the Administration's, chiefly because of lower expected corporate tax refunds. Other reestimates reflect different projections of interest receipts from Treasury's tax and loan accounts at commercial banks and from intragovernmental interest. The latter are offset in other budget functions and have no net effect on the deficit.

FUNCTION 920: ALLOWANCES

MAJOR SPENDING CHANGES PROPOSED FOR BUDGET FUNCTION 920:
ALLOWANCES (By fiscal year, outlays in billions of dollars)

Item	1988	1989	1990	1991	1992	Cumulative Five-Year Changes
CBO Baseline	0.9	3.3	5.7	8.6	11.6	
Proposed Changes						
Civilian agency pay raises	-0.6	-1.5	-2.5	-4.0	-5.5	-14.0
Davis-Bacon and Service Contract reforms	-0.1	-0.1	-0.2	-0.2	-0.2	-0.8
Credit reform initiative	-1.3	-0.6	0.9	2.2	3.6	4.8
Federal share of employee health premiums	-0.1	-0.2	-0.2	-0.3	-0.3	-1.1
Productivity savings	<u>--</u>	<u>-0.2</u>	<u>-0.5</u>	<u>-0.8</u>	<u>-1.0</u>	<u>-2.5</u>
Total	-2.1	-2.6	-2.5	-2.9	-3.4	-13.6
President's 1988 Budget as Estimated by CBO	-1.2	0.7	3.2	5.7	8.2	
President's 1988 Budget	-0.8	0.5	2.8	4.9	7.1	
CBO Reestimates	-0.4	0.2	0.5	0.8	1.1	2.1

Proposed Policy Changes

The allowances function contains several proposals affecting pay levels, benefit contributions, and other personnel practices concerning employees of civilian agencies. It also includes the President's credit reform initiative and reform of the Davis-Bacon and Service Contract Acts.

Civilian Agency Pay Raises. The Administration is proposing to limit pay rate increases to 2 percent in 1988 and 3 percent in 1989 through 1992 for white- and blue-collar civilian employees, effective in January for white-collar employees and at various times throughout the year with a three-month delay for blue-collar employees. The Administration, however, requests only one-half of the amount necessary to fund the proposed increase in 1988. Thus, civilian agencies would be required to pay for 50 percent of the 1988 pay raise from funds appropriated for other purposes. On the other hand, the Administration requests funding of the total cost of the 1988 pay raise for all Department of Defense (DoD) employees, shown in the national defense function (050). Coast Guard and Public Health Service officers would receive the same increases as DoD uniformed military employees: 4 percent in 1988, 4.3 percent in 1989, 4.6 percent in 1990, 4.5 percent in 1991, and 4.2 percent in 1992, effective each year in January.

The CBO baseline assumes pay rate increases equal to the annual rate of projected growth in private-sector pay: 3 percent in January 1988, 4.8 percent in October 1988, 5.2 percent in October 1989, 5.8 percent in October 1990, and 5.7 percent in October 1991. CBO estimates that the Administration's proposal would reduce outlays by \$0.6 billion in 1988 and by a total of \$14.0 billion in the 1988-1992 period, compared with the CBO baseline.

Reform of Davis-Bacon and Service Contract Acts. The Davis-Bacon and Service Contract Acts require that prevailing local wages be paid to workers hired by contractors involved in all federally funded or assisted projects above certain thresholds--\$2,000 for Davis-Bacon and \$2,500 for Service Contract. The Administration proposes to increase the minimum contract size subject to the requirements of the Davis-Bacon and the Service Contract Acts. The new thresholds would be \$1 million for Department of Defense contracts and \$100,000 for other agencies. These increases would allow contractors on smaller projects to pay lower wages in some cases. This change would result in lower contract costs, reducing outlays by about \$0.1 billion in 1988 and by a total of \$0.8 billion in the 1988-1992 period.

Credit Reform Initiative. The Administration is proposing to change the way federal credit programs are treated in the budget. At present, loan disbursements are scored as outlays and loan repayments are recorded as offsetting collections. Loan guarantee commitments appear in the budget only when a default occurs, and loan guarantee fees are treated as offsetting collections. Under the Administration's proposal, the budget would reflect the economic cost of these credit activities--the present value of the sub-

sidy, if any--in the year in which the direct loan or loan guarantee is made. The Administration's plan would reduce outlays by \$1.3 billion in 1988 and by \$0.6 billion in 1989, but would increase spending in later years. Chapter VII provides a further discussion of the Administration's credit proposals.

Government Contribution for Federal Employees Health Benefits (FEHB).

The Administration is proposing to lower the government's share of its employees' health insurance premiums by changing the formula used to determine contributions. The proposal would tie the government's share of costs to the average of premiums in all FEHB plans rather than--as under current law--to the average of premiums in only the six largest, high-option plans. This proposal would shift some of the government's share of health insurance costs to its employees and reduce outlays by \$0.1 billion in fiscal year 1988 and by a total of \$1.1 billion in the 1988-1992 period. About one-third of the total savings of this plan relates to lower government contributions for annuitants and is shown in the health function (550).

Productivity Savings. The Administration is proposing several changes in personnel policies which, it argues, would increase productivity. These proposals include replacing the virtually automatic within-grade increases for federal employees with merit increases based on employee performance and simplifying the pay and personnel systems. These proposals, which would take effect in fiscal year 1989, would reduce outlays by \$0.2 billion in 1989, and by a total of \$2.5 billion in the 1989-1992 period.

CBO Reestimates

Under CBO reestimates of the Administration's civilian agency pay raise proposals, outlays would be lower by \$0.3 billion in 1988, but would increase thereafter, for a total increase of \$2.3 billion in the 1988-1992 period. These outlay variations result from differences in estimates of payroll, the cost of the Quadrennial Commission pay raises for Judges, Members of the Congress, and other executives, and other estimating factors.

The budget omits the savings that result from the proposed changes in the Service Contract Act. Including CBO's estimates of these savings and of Davis-Bacon savings lowers projected outlays by \$0.1 billion in 1988 and by a total of \$0.2 billion in the 1988-1992 period. Other CBO outlay estimates do not differ significantly from the Administration's estimates for this function.